



THE CITY OF SAN DIEGO
MANAGER'S REPORT

DATE ISSUED: September 23, 2004

REPORT NO. 04-213

ATTENTION: Honorable Mayor and City Council
Docket of September 28, 2004

SUBJECT: Vinson and Elkins Report on Investigation
City Council Docket of September 21, 2004

SUMMARY

Issue - Should the City Council adopt the proposed ordinance contained in the report?

Manager's Recommendation – Adopt the proposed ordinance.

FISCAL IMPACT

The fiscal impact of the ordinance and other recommendations cannot be determined at this time. The staffing and other resource requirements will need to be assessed and brought back to City Council as they are implemented or they will be folded into the budgetary process.

BACKGROUND

The City Council engaged the firm of Vinson and Elkins L.L.P. (V&E) to review the City's disclosure practices from January 1996 through February 2004 and to investigate whether the City failed to meet disclosure obligations concerning its funding of SDCERS. On September 21, 2004, V&E concluded its evaluation and presented a report and recommendations to the City Council.

V&E's proposed ordinance and other recommendations are set forth in this report as Attachment 1. In addition to the proposed ordinance, the report comments on the other recommendations.

CITY MANAGER'S RECOMMENDATIONS

The V&E recommendations clearly provide all concerned with greater opportunity for input and review of disclosure materials throughout the bond document development and review process. I am confident that implementing these recommendations, coupled with an already initiated and ongoing change in City management culture, will insure that we produce full, complete and accurate disclosure going forward.

I agree wholeheartedly with the recommendations contained in the V&E Report and, in support of those recommendations, make the following observations:

1. The establishment of a Financial Reporting Oversight Board will be one factor that will restore "the integrity of the City's financial statements." (page 163) I believe that the scope of duties envisioned and recommended are both comprehensive and appropriate. Especially important is this board's role in hiring an outside auditor, reviewing the qualifications and work product of the outside auditor, and in providing a mechanism for confidential employee communication with the Board. I recommend that the Mayor and Council proceed with the appointment of the three member board.
2. The establishment of a Disclosure Practices Working Group (DPWG) will insure City compliance "with federal and state securities laws and to promote the highest standards of accuracy in disclosures relating to securities issued by the City." This recommendation will greatly enhance our existing procedures and strengthen controls. I embrace the opportunity to implement the recommendations of this group, and assist in shaping City disclosure practices and procedures which I anticipate will be a model for disclosure practices across the nation.

The DPWG would also be responsible for conducting mandatory training on disclosure issues. As an interim measure, the City's disclosure counsel conducted such sessions for over 100 City staff during the week of September 20th, and the City Attorney's Office is in the process of arranging similar training for the Mayor, Councilmembers and their staff.

I and City staff will work with the City Attorney and City Auditor to implement DPWG immediately and to conduct a thorough review of current disclosure practices in order to provide recommendations by December 1, 2004.

The report makes clear that the application of additional resources will be necessary to effectively implement V&E's recommendations. This is a key issue, in that City employees are routinely asked to do more with less. As the City enters the capital markets, its disclosure obligations have expanded and will undoubtedly continue to expand. With no added staff resources being applied to the growing workload, we could create expectations that we are unable to achieve. Given the importance of effectively

implementing V&E's recommendations, I intend to first fully analyze resource needs and make any necessary budgetary requests to adequately staff these functions.

3. Staffing resources in the City Attorney's office have thinned in recent years, particularly those dedicated to public finance issues. V&E recommends designating at least three Deputy City Attorneys to be responsible for the Financial Reporting Oversight Board, the DPWG and general supervision of finance and disclosure. Adding or redirecting experienced resources for this purpose is essential to timely issue resolution and critical to thorough document development and review.
4. Offering document certifications should be provided personally to the City Council by the City Manager and the City Attorney in conjunction with any request for City Council approval, since such certifications will increase both accuracy and accountability. The City Auditor would also provide a certification upon issuance of the City's Comprehensive Annual Financial Report (CAFR) and in connection with the incorporation of the CAFR in any disclosure document. In the absence of the City Manager or the City Attorney, the certifications could be provided by an authorized designee. However, given legal ramifications of such certifications, it is recommended the City Council afford the City Manager, City Attorney and assigned designees access to personal counsel in connection with this responsibility.
5. Disclosure documents should not be docketed on consent agendas – City staff has already acted to discontinue this practice and is ensuring that disclosure documents are placed on the adoption agenda, where they are assured of an opportunity for discussion.
6. The City should rely on a single, well-qualified firm to provide disclosure counsel services. The City has, in fact, already retained Hawkins Delafield and Wood, LLP, to do just that. I am a strong advocate for, and have previously discussed with current disclosure counsel the need for a complete review of all language in the City's disclosure documents, with the goal of ensuring that each statement is appropriately inclusive, and that its source can be identified.
7. While not a specific V&E recommendation, it's my view that both the goal of producing full, complete and accurate disclosure and the equally important goal of providing the City Council with useful budgetary assessment tools can be materially furthered by quantifying the short to medium term impact on the City's budget during "meet and confer" proposals, and by establishment of a pension unit within the Financial Management Department. These two actions would provide the Council with the fiscal impact of "meet and confer" items for not only the ensuing fiscal year, but for several years into the future, and would provide the staffing necessary to develop critical pension-related projections, including funding levels and contribution rates, and to provide the Council with the impact of those projections on a similar short to medium term basis as well.

CONCLUSION

It is my recommendation that the City Council proceed to implement the Vinson & Elkins recommendations, including the additional recommendations outlined in this report.

Respectfully submitted,

P. Lamont Ewell
City Manager

Note: The attachment is available for review in the Office of the City Clerk.

Attachment 1: Vinson and Elkins proposed ordinance and other recommendations.